89-1936 (1)

No. ____________

IN THE

Supreme Court of The United States

OCTOBER TERM, 1989

KARL and LUCILLE STEVENS
Petitioners

v.

STATE TAX ASSESSOR
Respondent

**PETITION FOR A WRIT OF CERTIORARI
TO THE
SUPREME JUDICIAL COURT OF MAINE**

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QUESTIONS PRESENTED

I. Whether the State of Maine's progressive income tax system violates the due process clause of the Fourteenth Amendment of the United States Constitution when applied to nonresidents, in that a nonresidents' non-Maine source income is considered in determining the rate of taxation, thereby subjecting the nonresidents' non-Maine source income to Maine's income tax?

II. Whether the State of Maine's progressive income tax system violates the equal protection clause of the Fourteenth Amendment or the privileges and immunities clause (Article IV, section 2) of the United States Constitution by taxing nonresidents at a higher effective tax rate than similarly-situated Maine residents?

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PETITION FOR A WRIT OF CERTIORARI
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The petitioners, Karl and Lucille Stevens, respectfully request that this Court grant the petition for writ of certiorari, seeking review of the Maine Supreme Judicial Court's opinion in this case.

OPINIONS BELOW

The opinion of the Supreme Judicial Court of Maine, which appears in the appendix hereto, p. 1a, *infra*, is reported at 571 A.2d 1195 (1990).

The opinion of the Kennebec County Superior Court, dated June 19, 1989, is not reported. It is reprinted in the appendix hereto, p. 6a, *infra*.

The decisions of the State Tax Assessor denying the petitioners' income tax refund claim and motion for reconsideration, dated July 15, 1988, and September 14, 1988, respectively, are not reported. They are reprinted in the appendix hereto, pp. 14a, 15a, *infra*.

JURISDICTIONAL STATEMENT

Karl and Lucille Stevens, petitioners, petition for review of the final judgment of the Supreme Judicial Court of Maine, dated March 15, 1990, holding that Me.Rev.State.Ann. tit. 36, §5111(4) (1985), *as amended by* Public Laws 1987, ch. 504, §7, as applied in this case, is not unconstitutional as being violative of petitioners' due process, privileges and immunities, and equal protection rights under the United States Constitution.

The jurisdiction of this Court to review the judgment of the Maine Supreme Judicial Court is invoked under 28 U.S.C. §1257(a).

CONSTITUTIONAL PROVISIONS AND STATUTES

Article IV, section 2, United States Constitution:

> The Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in the several States.

Article XIV, section 1, United States Constitution:

> All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any

> State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

Me.Rev.State.Ann., tit. 36, §5111(4) (1985), *as amended by* P.L. 1987, ch. 504, §7.

> [a] tax is imposed upon the Maine income of every nonresident individual. The amount of the tax shall be equal to the tax computed under this section and chapter 805 as if the nonresident were a resident, less applicable tax credits ... and multiplied by the ratio of his Maine adjusted gross income ... to his entire federal adjusted gross income, as modified by section 5122.
>
> [This section has been repealed and replaced by a new section 5111. See P.L. 1987, ch. 819, §2 (effective Jan. 1, 1988).]

STATEMENT OF THE CASE

In 1986, the State of Maine amended its graduated personal income tax statute, effectively increasing the taxes paid by nonresidents. The amendments require nonresidents to calculate their state income tax rate based upon their entire federal adjusted gross income, including income earned from sources outside of Maine. Because Maine has a graduated income tax, the result is that the percentage rate at which a nonresident is taxed is based upon his entire income, including non-Maine source income. This higher tax rate is then applied to the nonresident's Maine source income to determine the tax owed.

Karl and Lucille Stevens, petitioners, were married and residents of New Hampshire during 1986. Mr. Stevens was employed in Maine and earned wages of $32,179. Mrs. Stevens

was employed in New Hampshire and earned wages of $15,049. Petitioners also realized a capital gain in 1986 of $8,058 from the sale of real property located in New Hampshire, and received taxable interest and dividend income of $1,388 (none of which was from a Maine source). Petitioners first calculated their Maine tax liability in accordance with the amended law, and filed a joint nonresident Maine income tax return for 1986. Thereafter, petitioners filed a timely claim for refund for overpayment of taxes in the amount of $681, based upon an amended return that excluded all non-Maine source income. Petitioners' constitutional challenges were rejected by the State Tax Assessor, whose decision was upheld by the Kennebec County Superior Court and the Maine Supreme Judicial Court.

The federal questions sought to be reviewed were raised in the following manner. In petitioners' original claim for refund of overpayment of 1986 Maine state income taxes, petitioners alleged that Me.Rev.Stat.Ann., tit. 36, §5111(4) violates their "rights under the Due Process Clause (14th Amendment) of the U.S. Constitution" because Maine's system of taxing nonresidents results in the taxation of "income over which [Maine] has no jurisdiction." *Claim For Refund of Overpayment of 1986 Maine State Income Taxes* at 3. Petitioners further alleged that the same statute violated their "rights under the Equal Protection and Privileges and Immunities (Article 4, §2) clauses of the U.S. Constitution...." *Id.* at 4.

These claims were reiterated in petitioners' Motion for Reconsideration, filed with the State of Maine Bureau of Taxation. They were again raised in petitioners' Petition for Review of Final Agency Action, filed in Kennebec County Superior Court, and were all specifically addressed and rejected by the Superior Court, p. 6a, *infra*. They were also raised in petitioners' appeal to the Supreme Judicial Court of Maine, and were also specifically considered and rejected by that court, p. 1a, *infra*.

REASONS FOR GRANTING THE WRIT

The question of whether one state may indirectly tax income of nonresidents earned in another state is an important question of federal constitutional law. It is well-settled that a state's power to tax the income of nonresidents extends only to income derived from sources within the state. *See Shaffer v. Carter*, 252 U.S. 37, 57 (1920); *see also Travis v. Yale and Towne Mfg. Co.*, 252 U.S. 60 (1920). Undoubtedly, if Maine had sought to impose its tax directly upon petitioners' New Hampshire income, the tax would have been summarily struck down for violating due process.

Maine has been allowed by the state courts, however, to do indirectly what it plainly could not do directly. Maine takes into account nonresidents' non-Maine source income so as to increase their Maine tax liability. In this case, petitioners must pay an additional $681 in income tax to Maine solely because they received income from New Hampshire sources. Had petitioners earned exactly the same amount of income in Maine, but earned no New Hampshire income, then their tax bill from Maine would have been decreased by $681. It is apparent, therefore, that Maine is effectively taxing petitioners' activities in New Hampshire when it increases their Maine tax bill as a direct result of those activities.

> When property outside the state is taken into account for the purpose of increasing the tax upon property within it, the property outside is taxed in effect, no matter what form of words may be used.

Maxwell v. Bugbee, 250 U.S. 525, 544 (1919) (Holmes, J., dissenting) (5-4 decision).

Oliver Wendell Holmes' dissent in *Maxwell* foreshadowed this Court's recent emphasis in the state taxation field upon "the practical effect of a challenged tax," *Mobil Oil Corp. v.*

Commissioner of Taxes, 445 U.S. 425, 443 (1980), and upon "economic realities," *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). As demonstrated above, the practical effect of Maine's income tax scheme is to tax petitioners' New Hampshire income in violation of the due process clause.[1]

The majority in *Maxwell*, the main case relied upon below, upheld a New Jersey inheritance tax which looked to property beyond its jurisdiction as the basis for increasing the tax rate upon property subject to the tax:

> It is not to be disputed that, consistently with the Federal Constitution, a State may not tax property beyond its territorial jurisdiction. But the subject matter here regulated is a privilege to succeed to property which is within the jurisdiction of the state.

Maxwell, 250 U.S. at 539; *see also Great Atlantic and Pacific Tea Co. v. Grosjean*, 301 U.S. 412 (1937) (state tax upon "privilege" of operating chain stores). This theory — that a tax on a "local privilege" need not be scrutinized for its extraterritorial effects because the subject of the tax lies within the state's taxing power — may have been acceptable constitutional doctrine in 1919 and 1937. *But cf. Frick v. Pennsylvania*, 268 U.S. 473, 495 (1925) (*Maxwell* "is on the border line"). But that doctrine has been discredited by this Court's contemporary opinions in the state tax area, requiring practical analysis of state taxes and rejecting the formalistic doctrine upon which cases

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[1] Petitioners' equal protection and privileges and immunities arguments essentially rise and fall with the due process argument. Petitioners contend that a nonresident and Maine resident are similarly situated if they have the same Maine source income; respondent looks to petitioners' total income (including non-Maine source income). Petitioners contend that looking to a nonresidents' non-Maine source income is unreasonable because that income lies beyond Maine's taxing jurisdiction.

like *Maxwell* and *Grosjean* were predicated.[2] *See, e.g., American Trucking Associations, Inc. v. Scheiner*, 483 U.S. 266 (1987) (overruling *Aero Mayflower Transit Co. v. Georgia Public Service Comm'n*, 295 U.S. 285 (1935), *Aero Mayflower Transit Co. v. Board of Railroad Commissioners*, 332 U.S. 495 (1947), and *Capitol Greyhound Lines v. Brice*, 339 U.S. 542 (1950), which held that flat taxes on interstate trucks were valid under the commerce clause in part because they were imposed on a "local privilege"); *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981) (overruling *Heisler v. Thomas Colliery Co.*, 260 U.S. 245 (1922), which held that a tax on a "local privilege" was immune from commerce clause scrutiny); *Western and Southern Life Insurance Co. v. State Board of Equalization*, 451 U.S. 648 (1981) (overruling *Lincoln National Life Insurance Co. v. Read*, 325 U.S. 673 (1945), which held that the equal protection clause did not protect out-of-state insurers until they had been admitted to do a "local" business in the state); *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977) (overruling *Spector Motor Service, Inc. v. O'Connor*, 340 U.S. 602 (1951), which held that a tax on a "privilege" of doing interstate business was *per se* unconstitutional); *Michelin Tire Corp. v. Wages*, 423 U.S. 276 (1976) (overruling the formalistic doctrine that the import-export clause protected goods from taxation so long as they were in their "original packages"); *Japan Line, Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979) (abandoning the anachronistic

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[2] Also decided before this Court's contemporary decisions in the state tax area was *Wheeler v. State*, 249 A.2d 887 (Vt.), *appeal dismissed for want of a substantial federal question*, 396 U.S. 4 (1969). *Wheeler* involved a challenge similar to the instant case to Vermont's income tax as applied to nonresidents. In essence, the Vermont Supreme Court simply followed *Maxwell* and *Grosjean*. This Court's summary dismissal of the appeal, while having precedential value, *see Hicks v. Miranda*, 422 U.S. 332, 343-45 (1975), is not "of the same precedential value as would be an opinion of this Court treating the question on the merits.'" *Tully v. Griffin, Inc.*, 429 U.S. 68, 74 (1976) (quoting *Edelman v. Jordan*, 415 U.S. 651, 671).

"home port" doctrine incorporated into the Court's due process and commerce clause jurisprudence as a jurisdictional limitation on state taxation).

The "practical effect" of Maine's unfair nonresident tax scheme extends beyond its confiscatory effect upon New Hampshire residents.[3] New Hampshire residents subject to this unfair tax have no representation in the legislature of the state imposing it. If Maine continues to pick the pockets of New Hampshire residents, retaliatory actions by the state of New Hampshire may be inevitable. For example, in addition to authorizing the state attorney general to represent petitioners in this action, *see* N.H. Laws 1987, ch. 157, the New Hampshire legislature in 1989 refused to enter into future agreements concerning the legal length of lobsters with the state of Maine unless Maine repeals the provisions of the Maine personal income tax statutes "which impose, assess, or collect from residents of this state unjust taxes, the so-called 'spousal tax.'" N.H. Laws 1989, ch. 78:4. One of the chief ends sought to be accomplished by the adoption of the Constitution was preventing just that sort of retaliation. *See Austin v. New Hampshire*, 420 U.S. 656, 667 (1975).

The citizens of New Hampshire have chosen not to enact a general, personal income tax. Her neighbors (Maine and Vermont) have taken advantage of this policy decision by enacting graduated personal income taxes that increase the taxes of New Hampshire residents as a direct result of their New Hampshire income. Because New Hampshire has no such income tax, her neighbors need not be concerned about losing tax revenues from residents due to tax credits resulting from a New Hampshire income tax. The State of New Hampshire

[3] The financial impact upon nonresidents is substantial. The Fiscal Note attached to the 1986 bill amending Maine's income tax estimated increased revenues for 1986-87 of approximately 3½ million dollars would result.

should not be required to enact a discriminatory graduated income tax in order to recover back from Maine residents taxes that would offset the discriminatory taxes collected from New Hampshire residents by the State of Maine. New Hampshire's decision not to enact an income tax is intended to benefit her citizens, not the treasuries of her neighboring states. The due process clause should prevent Maine from taxing the New Hampshire income of New Hampshire residents.

CONCLUSION

For these reasons, this petition for certiorari should be granted.

Respectfully submitted,

KARL AND LUCILLE STEVENS

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MAINE SUPREME JUDICIAL COURT

Reporter of Decisions
Decision No. 5381
Law Docket No. Ken-89-330

KARL and LUCILLE STEVENS

v.

STATE TAX ASSESSOR

Argued January 30, 1990
Decided March 15, 1990

Before WATHEN, GLASSMAN, CLIFFORD, HORNBY and COLLINS, JJ.

CLIFFORD, J.

This appeal challenges the method used by the State of Maine in taxing the Maine source income of nonresidents. Because there are no constitutional violations resulting from Maine's taking into account non-Maine source income in calculating the graduated rate of income tax to be imposed on the nonresident's Maine source income, we affirm the judgment of the Superior Court (Kennebec County, *Brody, C.J.*) upholding the defendant State Tax Assessor's denial of a tax refund to plaintiffs, Karl and Lucille Stevens.

The Stevenses, husband and wife, are residents of New Hampshire. During 1986, Karl Stevens earned income in Maine at the Portsmouth Naval Shipyard in Kittery, while Lucille Stevens worked in New Hampshire. The Stevenses also reported interest, dividend and capital gain income from non-Maine sources. After calculating their Maine tax liability in accordance with the law and filing a joint nonresident Maine income tax return for 1986, the Stevenses filed a claim for a

refund for overpayment of taxes.[1] The refund was denied by the State Tax Assessor as was a petition for reconsideration. *See* 36 M.R.S.A. §§5280, 151 (1978 & Supp. 1989). The Assessor's denial of the refund was affirmed in the Superior Court in the action brought by the Stevenses pursuant to 5 M.R.S.A. §11002(1) and M.R. Civ. P. 80C. Their appeal to this court followed.

Maine's income tax law has graduated or progressive features, with the applicable rates at which taxes are calculated increasing as the amount of the taxpayer's income increases. *See* 36 M.R.S.A. §5111 (Supp. 1989). Maine income taxes paid by a nonresident taxpayer are subject to the graduated tax rate. The graduated scheme of taxation is implemented by calculating the tax rate upon the nonresident's entire federal taxable income, and applying that rate to the Maine source income of the nonresident. Specifically, the graduated rate is determined by reference to the federal adjusted gross income (less deductions and exemptions) and the tax, so calculated, is reduced by the ratio of the non-Maine source income to the total income.[2]

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[1] The refund claim for $681, based upon an amended return that excluded all non-Maine source income, was filed through the Office of the Attorney General of the State of New Hampshire. The Stevenses continue to be represented by the Attorney General of New Hampshire in this appeal.

[2] The statute applying to 1986 tax returns, 36 M.R.S.A. [5111(4) (1985), *as amended by* P.L. 1987, ch. 504, §7, provided that:

> [a] tax is imposed upon the Maine income of every nonresident individual. The amount of the tax shall be equal to the tax computed under this section and chapter 805 as if the nonresident were a resident, less applicable tax credits ... and multiplied by the ratio of his Maine adjusted gross income ... to his entire federal adjusted gross income, as modified by section 5122.

36 M.R.S.A. §5111(4) has been repealed and replaced by a new section 5111. *See* P.L. 1987, ch. 819, §2 (effective Jan. 1, 1988).

The well-established right of the State of Maine to tax income earned within its borders by a nonresident is not challenged by the Stevenses. *Barney v. State Tax Assessor*, 490 A.2d 223, 225 (Me.), *cert. denied*, 474 U.S. 828 (1985); *Morse v. Johnson*, 282 A.2d 597, 599-600 (Me. 1971). The Stevenses' contention is that inclusion of their non-Maine source income to determine the rate at which their Maine income is to be taxed violates their due process,[3] privileges and immunities,[4] and equal protection[5] rights under the Constitution of the United States. That contention has been squarely addressed and clearly rejected. *See Maxwell v. Bugbee*, 250 U.S. 525, 538-43 (1919); *see also Wheeler v. State*, 249 A.2d 887, 890-91 (Vt.), *appeal dismissed for want of a substantial federal question*, 396 U.S. 4 (1969)(per curiam). We reject it as well.

In *Maxwell*, the United States Supreme Court upheld the authority of a state (New Jersey) to base an inheritance tax rate to be applied to property, subject to its jurisdiction upon all property of the estate, including property that could not lawfully be taxed. *Id.* at 539-40. "When the State levies taxes within its authority, property not in itself taxable by the State may be used as a measure of tax imposed." *Id.* at 539.

Courts of other jurisdictions have applied this principle to the computation of a nonresident's state income taxes. In *Wheeler*, a case strikingly similar to the instant one, Vermont's nonresident graduated tax rate, determined upon the total taxable income of nonresidents, including non-Vermont source income, was applied to the Vermont source income of Wheeler, a New Hampshire resident. Wheeler's Vermont source income comprised 25 percent of his total income. *Id.* at

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[3] U.S. Const. amend. XIV.

[4] U.S. Const. art. IV, §2.

[5] U.S. Const. amend XIV.

890-91. Wheeler's constitutional contentions, identical to those made by the Stevenses, were rejected first by the Vermont court and later by the United States Supreme Court, which dismissed the case for want of a substantial federal question, a disposition that the Stevenses concede has the precedential effect of a decision on the merits. *Hicks v. Miranda*, 442 U.S. 332, 343-35 (1975).

Similar constitutional attacks were likewise rejected in *United States v. Kansas*, 810 F.2d 935 (10th Cir. 1987). "The reasoning of the[se] cases [upholding taxation schemes similar to Maine's] is that property not itself taxable can be used as a measure of the tax imposed on property within the state and that to do so is 'in no just sense a tax on the foreign property.'" *Id.* (quoting *Maxwell*, 250 U.S. at 539)(discussing and dismissing due process violations).

The State's taxation of the Stevenses does not deprive them of their property without due process. Nor does it violate their constitutionally protected privileges and immunities or deny them equal protection of the law. Privileges and immunities and equal protection rights would be implicated only if the State's income tax scheme discriminated against nonresidents when compared to residents similarly situated. *Barney*, 490 A.2d at 225; *Wheeler*, 249 A.2d at 889-91. Although the Stevenses point out that they paid more Maine income tax on their Maine source income than a Maine resident whose *total* income equals the Stevenses' Maine source income (because the Stevenses paid at a higher graduated tax rate), their comparison misses the mark. There is no improper discrimination in the application of Maine's income tax because similarly situated residents and nonresidents are taxed at an equal rate. The tax rate applied to residents with gross incomes identical to that of the Stevenses would be the same as that paid by the Stevenses. Unlike the Stevenses, however, who paid taxes on

only their Maine source income, Maine residents would have that rate applied to all of their adjusted gross income regardless of the source.[6]

The entry is:

Judgment affirmed.

All concurring.

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[6] Were the Stevenses residents of Maine, a state income tax of $2812, or 4.96 percent of their federal adjusted gross income of $56,674, would have been due. As nonresidents, the Stevenses paid $1596, or 4.96 percent of their Maine source income of $32,179.

STATE OF MAINE KENNEBEC, ss

SUPERIOR COURT CV-88-367

KARL & LUCILLE STEVENS,)

PETITIONERS)

v. ORDER

STATE TAX ASSESSOR,)

RESPONDENT)

This matter is before the court on petition of Karl and Lucille Stevens (Stevenses), residents of New Hampshire, for reversal of the decision of the State Tax Assessor of the State of Maine (Assessor) denying petitioners' claim for a refund for overpayment of 1986 Maine state income taxes. Briefs and an Agreed Statement of Facts have been presented, and oral argument was heard on June 8, 1989.

FACTS:

The Stevenses are a married couple residing in Rochester, New Hampshire. Throughout 1986, Karl Stevens was employed at the Portsmouth Naval Shipyard in Kittery, Maine, and his wife was employed in Rochester, New Hampshire. The Stevenses timely filed a joint 1986 Maine state income tax form in which, pursuant to instructions accompanying the tax form, the couple set forth their 1986 adjusted gross income as identified by them in their 1986 federal income tax return. The income so listed included Lucille Stevens' earnings from her New Hampshire job, and other "non-Maine derived" income. In accordance with the appropriate form, they calculated the Maine income tax they would have been obligated to pay were they Maine residents; but, following instructions given in the "Non-Resident Schedule" they then calculated a

credit which reflected the ratio of their Maine adjusted gross income to their total adjusted gross income, and applied this credit to their previously calculated Maine tax obligation. The result was their final Maine tax obligation, as non-residents, of $1,596, which they duly paid.

Thereafter, the Stevenses challenged the validity of the Maine statutory requirement 36 M.R.S.A. §5111(4) imposed by a 1986 amendment to Maine Personal Income Tax statutes (P.L. 1986, Ch. 783), setting out the mode described above by which non-residents calculate their Maine tax obligation. They effected this challenge by filing an amended Maine Form 1040-E for 1986, listing once again the amount of adjusted gross income they had reported on their federal form, but going on to claim an offset, in the form of an "income modification," which amounted to the Stevens' non-Maine derived income. They then proceeded to calculate their Maine tax obligation. Consistent with this procedure they did not indicate a "non-resident credit," because, as they explained, "the 'non-resident credit' is thus 100% of non-Maine income, and is treated here as an income modification." (*Petitioners' Brief, Exhibit C — Attachment.)*

Petitioners' revised method effectively reduced the adjusted gross income on the basis of which they eventually calculated their tax obligation. Under the method called for in §5111(4), and which the Stevenses had originally used, the tax obligation was calculated beginning with a higher adjusted gross income figure, which included all the Stevens' non-Maine income. The Stevenses claim the $681 they calculate as the difference between the results of their first and second calculations. Their refund claim was denied by the Assessor, as was their petition for reconsideration of the denial.

In addition to making claim to the $681, petitioners also ask that P.L. 1986, ch. 783, the chapter of the Maine statutes setting out the calculation method to which they object, be de-

clared unconstitutional. They argue that its provisions deprive them of rights guaranteed by the federal and Maine constitutions. In particular they point to the federal 5th and 14th Amendment due process clauses, the federal 14th Amendment equal protection clause, and the federal Privileges and Immunities clause, Art. IV, §2. In submitting their amended tax form they made clear they were setting out the revised calculation despite the fact that their approach did not reflect "the current state of the statutory law," and that the calculation of tax obligation was accurate "only in the context of the constitutional challenge." (*Petitioners' Brief, Exhibit B — Attachment.)*

DISCUSSION:

The power of Maine to tax the income received by non-residents employed in Maine is well-settled as being within national and state constitutional limits. *Barney v. State Tax Assessor*, 490 A.2d 223 (Me. 1985); *Morse v. Johnson*, 282 A.2d 597 (Me. 1971); *Travis v. Yale & Towne Mfg. Co.*, 252 U.S. 60, 75-76 (1920). The power of Maine to tax the income of Maine residents earned outside the state is also clear. *Opinion of the Justices*, 255 A.2d 655 (Me. 1969). Also settled is the proposition that the power of Maine to tax the income of non-residents is defined by the reach of Maine's *in rem* and *in personam* authority. *Shaffer v. Carter*, 252 U.S. 37, 49 (1920).

There is sparse case law or scholarly commentary on the precise question posed in this case. But reasoning by courts dealing with analogous issues, and in one case with a very similar factual situation, furnishes strong evidence of agreement on basic principles.

This case presents a variation of the problem focused on by the Law Court in *Barney v. Tax Assessor*, 490 A.2d 223 (Me. 1985). There the question was whether Maine, in determining a non-resident's tax liability, could relate the income earned by

him within Maine to income earned by him outside Maine without violating the Privileges and Immunities clause of the U.S. Constitution because it deprived the non-resident of a deduction or exemption to which he would have been fully rather than only proportionately entitled were he a Maine resident. The Law Court found no constitutional problem. *Id.* at 225; *cert. denied* 474 U.S. 828 (1985). The Law Court reasoned that prorating the extent of the non-resident's deductions and exemptions under Maine law according to the ratio of his out-of-state and Maine income reflected a reasonable estimate of the relationship of the non-resident to Maine's state government. The non-resident was "called upon to make no more than his ratable contribution to the support of the state government." *Id.* at 225, citing *Austin v. New Hampshiree*, 420 U.S. 656, 665 (1975). In the case before the Court, the non-resident Stevenses are "called upon" as non-resident beneficiaries of Maine state government to make a "ratable" contribution to the support of that government. Just as the relationship between the non-resident and Maine was expressed in *Barney* through the Maine income/total income ratio, so here the ratio also expresses the non-resident/state relationship. This time the emphasis is on "progressivity," i.e. varying "ability to pay," in the sharing of the burdens of state government services.

Whatever questions there might be about the constitutionality of the emphasis by the Maine tax code on progressivity, which is what is basically involved in Maine's insistence that non-residents begin calculating their Maine tax obligation by setting out their total federal adjusted gross income, there is no constitutional Privileges and Immunities prohibition. In *Barney*, the Law Court stressed that Maine's tax deductions and exemptions were neutral in their effect on residents and non-residents. Looking at any non-resident taxpayer's total income, it is clear that any variation between his effective rate and that of a similarly situated Maine resident will depend on

his own State's base rate and tax benefit policy. Privileges and Immunities doctrine requires no more than that.

With respect to due process, a two-pronged standard has emerged nationally for judging the constitutionality of the attempts of a state to take into consideration in one way or another the out-of-state earnings of a non-resident in determining his tax liability on income earned within the state. First, "due process requires some definite link, some minimum connection between a state and a person, property or transaction" it seeks to relate to its tax calculation. *Miller Bros. Co. v. Maryland*, 347 U.S. 340, 344 (1954). Second, there must be a "rational relationship" between the income attributed to the state for tax purposes and the "values connected with the taxing state." *Moorman v. Bair*, 437 U.S. 272, 273 91978). The U.S. Supreme Court has used this test in evaluating the validity of state income tax legislation relating corporate income earned by foreign corporations to the total net income of those corporations. *Mobil Oil Corporation v. Commissioner of Taxes of Vermont*, 445 U.S. 425 (1980), and *Exxon Corp. v. Wisconsin Dept. of Revenue*, 447 U.S. 207 (1980) stand for the principle among others that due process considerations do not prevent a state in its calculation of the tax obligation of a non-resident from placing the income earned by the non-resident in the context of his total earnings, intra and extra state, that is, all the net income of the corporation "under the laws of the United States," *Mobil Corp. v. Commissioner of Taxes of Vermont*, 445 U.S. 425, 429 (1980), and using that total earnings experience as the base from which to calculate the non-resident's tax obligation.

More nearly approaching the factual situation in this case is the recently-decided *United States v. Kansas*, 810 F.2d 935 (10th Cir. 1987), which evidences how broadly accepted is the validity of the technique used by Maine to determine the Stevens' Maine tax obligation. The United States had brought suit against the state of Kansas, objecting to Kansas' incorpo-

rating the military pay of a U.S. serviceman stationed at a military base in Kansas *ab initio* in calculating the serviceman's Kansas tax obligation on his non-military income earned in Kansas. The United States had argued that the Kansas action infringed national sovereignty by violating a provision of the Soldiers and Sailors Civil Relief Act of 1940, which prohibits state taxation of United States military compensation. Citing a line of cases going back to *Maxwell v. Bugbee*, 250 U.S. 525 91919), the Court of Appeals summarized the guiding principle involved as being that "...property not itself taxable can be used as a measure of the tax imposed on property within the state, and ... to do so is in no just sense a tax on the foreign property." *United States v. Kansas*, 810 F.2d 935, 938 (10th Cir. 1987), citing *Maxwell v. Bugbee*, 250 U.S. 525, 539 (1919). The Court said, "...the income in the taxing state is merely being taxed at an increased rate pursuant to a progressive system of taxation premised on the individual's ability to pay." *United States v. Kansas*, 810 F.2d 935, 938 (10th Cir. 1987), citing *Wheeler v. State*, 249 A.2d 887 (Vt. 1969), *appeal dismissed* 396 U.S. 4 (1969). While the United States had argued in its brief that "taxing nonmilitary income at rates which are higher due to the inclusion of military income in the rate-setting calculation constitutes a 'sophisticated scheme of indirect taxation,'" *at 936*, the Appeals Court held that "...the mere inclusion of military compensation in a formula determining the rate of tax on income from Kansas sources does not constitute a tax on the military income of a nonresident individual. *Id.* at 938.

While the action in *United States v. Kansas* was brought by the United States under the Supremacy Clause of the United States Constitution (Art. VI), the Appeals Court specifically noted that the United States had not pursued an equal protection argument, and had conceded that Kansas' action did not violate national due process rights of the serviceman. *Id.*

Progressivity is a key feature of the Maine tax code as it applies to Maine residents; Maine residents must report on their Maine tax returns all earned income from out-of-state sources as well as from those within Maine. Maine is not asking the Stevenses to do anything not being asked of its own residents. Under present Maine law Mr. Stevens was free to report his Maine-earned income as a single individual, with a single-individual tax rate then being applied. But the Stevenses chose the option provided by the final clause of 36 M.R.S.A. s. 5221(2): "...but they may elect to determine their joint taxable income as nonresidents, in which case their liabilities shall be joint and several." It is reasonable to assume that the Stevenses chose this option because it worked out to their financial advantage. Now they are asking in effect that they be allowed to ignore the statute so that Mr. Stevens' single individual return is transformed into a joint return including only his income, to be taxed at a reduced joint rate. The two prongs of the national due process standard appear eminently satisfied: At a minimum the filing by the Stevenses of a joint return provides that elemental connection "between a state and a person, property or transaction" spoken of in *Miller*, 347 U.S. 340 (1954); and the application of a progressive rate to Mr. Stevens' earnings is a rational objective of the state of Maine, attained logically by incorporating his wife's out-of-state income as set out in a joint tax return, not for purposes of taxing that income, but of treating Mr. Stevens' fairly when it comes to taxing his Maine earnings. The second prong of the national due process test is therefore satisfied, *Moorman v. Bair*, 437 U.S. 272, 273 (1978). Indeed, there would seem little doubt that Maine in evaluating Mr. Stevens' income for progressivity purposes would meet due process standards were it to require him to indicate out-of-state earnings of himself and his wife even in filing a return as a single individual.

In sum, the state of Maine is not taxing the New Hampshire income of the Stevenses. It is using the combined income tech-

nique as a way of determining the degree of progressivity to be attributed to Mr. Stevens' Maine income. Maine taxes Maine residents' incomes at variable rates. A Maine resident's locally-produced income is incorporated by way of the tax return into a common fund of his total earnings. This is done both in Mr. Stevens' case and in that of a Maine resident as part of the expression of the values of Maine society, which include the notion of "ability to pay" as an important part of Maine community values. Mr. Stevens enjoys the advantage of having his wife's income not being taxed by Maine. He is not disadvantaged in any equal protection sense in having his wife's New Hampshire income included simply as a way of measuring his capacity to contribute to the Maine community of which he is a part.

Therefore, it is hereby ORDERED:

There being in this case no deprivation of due process, equal protection or privileges and immunities rights of the petitioners, their petition is DENIED, and the decision of the State Tax Assessor denying the petitioners' request for a refund is AFFIRMED.

/s/ Morton A. Brody

June 29, 1989

MORTON A. BRODY
Chief Justice, Superior Court

BUREAU OF TAXATION

STATE OF MAINE
State Office Building

Augusta, Maine 04333
July 15, 1988

Karl and Lucille Stevens
35 Summer Street
East Rochester, New Hampshire 03867

SS #003-28-4157

RE:1986 Form 1040-ME. (Amended)

Dear Mr. and Mrs. Stevens:

Your refund claim for 1986 Maine individual income tax is denied. It is the Bureau of Taxation's position that the operation of the Maine Income Tax Law as it relates to your circumstances is appropriate and legal in all respects.

If you desire the State Tax Assessor to reconsider this denial of your application for refund pursuant to Title 36 M.R.S.A. §151, your written petition setting forth the grounds on which the denial is protested must be made within 15 days after receipt of this notice. Failure to request a reconsideration will terminate your right to court review of the refund denial.

If you have any questions, please feel free to contact me.

Sincerely,

Stephen J. Murray
State Tax Assessor

BY */s/ Jerome D. Gerard*

Jerome D. Gerard, CPA
Director of Maine Income Tax
Income Tax Section
Tel. (207) 289-3695

JDG:emm
CERTIFIED MAIL

BUREAU OF TAXATION

STATE OF MAINE
State Office Building
Augusta, Maine 04333

September 14, 1988

Robert E. Dunn, Jr., Esq.
Attorney, Civil Bureau
Office of the Attorney General
25 Capitol Street
Concord, New Hampshire 03301-6397

RE: Karl and Lucille Stevens
SS# 003-28-4157

Dear Mr. Dunn:

Your petition filed July 25, 1988, was timely filed under Title 36 MRSA §151, for reconsideration of the July 15, 1988 denial of the Stevens' claim for refund of 1986 income taxes.

The applicable law is Title 36 MRSA §§5111-4, 5220-2 and 5221-2, which sections pertain to nonresident individual income tax returns and the computation of tax.

In this case, Mr. and Mrs. Stevens are nonresidents who elected to file a joint Maine income tax return for 1986. Karl Stevens had Maine-source income in 1986, but Lucille Stevens had no Maine-source income in that year. They computed their tax on the basis of their Federal adjusted gross income and paid the tax. Subsequently, they filed a claim for refund of their 1986 income tax based on the exclusion of Lucille Stevens' income. The claim was denied on July 15, 1988.

Upon reconsideration, I have determined that the denial of the claim for refund must be sustained.

If you wish to appeal this decision, you must file a petition for review in Superior Court within thirty (30) days of receipt of this notice in accordance with Title 5, MRSA §11002.

Very truly yours,

Stephen J. Murray
State Tax Assessor

By: *_/s/ Rufus E. Stetson, Jr._*
Rufus E. Stetson, Jr., Director
Appellate Division
Tel. (207) 289-4134

RES:lsc

cc: Karl and Lucille Stevens

CERTIFIED MAIL

No. 89-1936

In the

Supreme Court of the United States

October Term, 1989

KARL AND LUCILLE STEVENS,

Petitioners,

v.

STATE TAX ASSESSOR,

Respondent.

**Petition for Writ of Certiorari
To the Supreme Judicial Court of Maine**

BRIEF IN OPPOSITION

JAMES E. TIERNEY
Attorney General

CLIFFORD B. OLSON
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State House Station #6
Augusta, ME 04333
(207) 289-3661

Attorneys for Respondent

July 20, 1990

COCKLE LAW BRIEF PRINTING CO., (800) 225-6964
OR CALL COLLECT (402) 342-2831

QUESTION PRESENTED

Is Maine's consideration of non-Maine income in computing the income tax rate to be applied to the Maine income of a nonresident taxpayer consistent with the Due Process Clause, the Privileges and Immunities Clause and the Equal Protection Clause of the Constitution of the United States?

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No. 89-1936

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**Petition for Writ of Certiorari
To the Supreme Judicial Court of Maine**

BRIEF IN OPPOSITION

STATEMENT OF THE CASE

Petitioners Karl and Lucille Stevens ("the Stevenses") at all relevant times were married and were domiciliaries of New Hampshire. For the entire year 1986, Karl Stevens was employed at the Portsmouth Naval Shipyard, a federal enclave located within the boundaries of the State of Maine, and Lucille Stevens was employed in the State of New Hampshire. The Stevenses also had interest, dividend and capital gain income from non-Maine sources.

Because they elected to file a joint Maine individual income tax return for 1986,[1] the Stevenses computed their Maine income tax liability as if they were Maine residents and were allowed, against that liability, a credit which reflected the ratio of their non-Maine adjusted gross income to their total adjusted gross income. 36 M.R.S.A. § 5111(4) (*repealed and replaced by* P.L. 1987, ch. 819, § 2).

In 1988, the Stevenses, represented by the New Hampshire attorney general's office, filed a claim for refund of a portion of their 1986 Maine income tax. The claim was based primarily upon the proposition that Maine's consideration of the Stevenses' non-Maine income in determining the tax rate to be applied to their Maine income constituted, in effect, a tax upon that non-Maine income in violation of the Due Process Clause (Amend. XIV, § 1) of the Constitution of the United States.[2] The Stevenses also asserted that the Maine computation method violated the Privileges and Immunities Clause (Art. IV, § 2, cl. 1) and the Equal Protection Clause (Amend. XIV, § 1) of the Constitution of the United

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[1] Mrs. Stevens' income was reported on this return only because the Stevenses elected to file jointly. 36 M.R.S.A. § 5221(2) (Supp. 1989). If he had chosen to do so, Karl Stevens could have filed a separate return under the rates applicable to single persons and married persons filing separately. *See* 36 M.R.S.A. § 5111(1) (Supp. 1989). He presumably chose not to do so because it was financially advantageous to file a joint return.

[2] $232 of the Stevenses' claimed overpayment of $681 was attributable to their unwarranted presumption that the Maine Income Tax Law would allow nonresidents full, rather than prorated, personal exemptions and deductions if their position in this litigation were sustained. *See Barney v. State Tax Assessor*, 490 A.2d 223 (Me.), *cert. denied*, 474 U.S. 828 (1985).

States. The State Tax Assessor denied the refund claim. On *de novo* appeal, the Kennebec County Superior Court held that Maine's computation method was constitutional. Petition for Writ of Certiorari ("Pet.") 6a-13a.

On appeal, the Supreme Judicial Court of Maine held that the Assessor's reference to the Stevenses' total income to determine the rate of tax to be applied to their Maine income did not violate the Due Process Clause. In addition, the court held that neither the Privileges and Immunities Clause nor the Equal Protection Clause had been violated because the Stevenses were taxed on their Maine income at the same rate at which similarly-situated Maine residents would have been taxed on their total income. *Stevens v. State Tax Assessor,* 571 A.2d 1195 (Me. 1990), Pet. 1a-5a.

REASONS FOR DENYING THE WRIT

The decision below is consistent with precedents of this Court and does not give rise to a substantial federal question.

The decision of the Supreme Judicial Court of Maine is consistent with long-established precedent of this Court and therefore does not merit review. In *Maxwell v. Bugbee,* 250 U.S. 525 (1919), this Court held that New Jersey had constitutionally determined inheritance tax liability with respect to a nonresident decedent by applying its graduated rates to the total property of the decedent and prorating the result by the ratio of the decedent's New Jersey property to his total property. In *Great Atlantic & Pacific Tea Co. v. Grosjean,* 301 U.S. 412 (1937), this Court, relying in part upon *Maxwell,* upheld a

Louisiana license tax statute under which the tax imposed upon each Louisiana chain store was dependent upon the total number of stores, both in-state and out-of-state, in the chain.

More recently, in 1969, this Court dismissed, for want of a substantial federal question, an appeal challenging an income tax statute almost identical to Maine's. *Wheeler v. State*, 249 A.2d 887 (Vt.), *decision adhered to*, 253 A.2d 136, *appeals dismissed*, 396 U.S. 4. *Cf. Davis v. Franchise Tax Board*, App., 139 Cal. Rptr. 797, 799 (1977), *appeal dismissed for want of a substantial federal question*, 434 U.S. 1055 (1978) (constitutionality of California's denial of income averaging to nonresidents was supported in part by California's having foregone its constitutional option of using their total income in its computation of tax on their California income).

The Stevenses now argue that *Maxwell, Grosjean* and *Wheeler* should be reexamined in light of what they describe as this Court's "recent" emphasis upon "economic realities" and the "practical effect" of taxes. Pet. 5-8. In fact, however, this Court's focus upon the practical effect of taxes is nothing new. Within months of its decision in *Maxwell*, for example, the Court stated the need to give less regard to "theoretical distinctions" and more to the "practical effect and operation" of an income tax statute as applied to nonresidents. *Shaffer v. Carter*, 252 U.S. 37, 56 (1920). Furthermore, this Court had no difficulty in overturning an inheritance tax when it actually taxed extraterritorial value. *Frick v. Pennsylvania*, 268 U.S. 473 (1925).

In support of their argument that *Maxwell, Grosjean* and *Wheeler* should be reexamined, the Stevenses primarily rely upon decisions under the Commerce Clause. The

analysis in those cases, however, is not relevant to the Stevenses' challenge here, which is primarily based upon the Due Process Clause. Moreover, the cases relied upon by the Stevenses all involve instances in which this Court has abandoned formalistic wooden doctrines which did not accurately reflect economic realities.

Thus, four of the six cases upon which the Stevenses rely relate to this Court's 1977 rejection of the long-standing commerce clause standard that a tax could not be directly imposed upon interstate commerce. *See Complete Auto Transit v. Brady,* 430 U.S. 274 (1977) (replacing old standard with new 4-prong test); *Japan Line, Ltd. v. County of Los Angeles,* 441 U.S. 434, 441-444 (1979) (continuing vitality of "home port doctrine" not determined because case could be decided under two additional foreign commerce prongs of new commerce clause test); *Commonwealth Edison Co. v. Montana,* 453 U.S. 609, 614-617 (1981) (immunization of tax on local event from commerce clause scrutiny is no longer necessary to protect state's taxing authority); *American Trucking Associations, Inc. v. Scheiner,* 483 U.S. 266, 292-296 (1987) (prior decisions upholding flat taxes for privilege of using a state's highways are no longer appropriate now that interstate commerce may be required to pay its way).

The other two authorities cited by the Stevenses similarly involved the overruling of anachronistic decisions and doctrines. *See Western & Southern Life Ins. Co. v. State Bd. of Equalization,* 451 U.S. 648, 662-668 (1981) (overruling *Lincoln Nat'l Life Ins. Co. v. Read,* 325 U.S. 673 (1945), which had been rendered an anachronism by equal protection decisions dating from 1910 through 1968); *Michelin Tire Co. v. Wages,* 423 U.S. 276 (1976) (overruling *Low*

v. Austin, 80 U.S. (13 Wall.) 29 (1871), which had wrongly decided that imports could not be taxed by states at all until they lost their character as imports). These cases offer no support for the Stevenses' argument that this Court should now review *Maxwell, Grosjean* and *Wheeler.*

In contrast to the cases overruled in the decisions cited by the Stevenses, the principle of *Maxwell* is not a "formalistic doctrine" (Pet. 6) but, rather, a mathematical reality. As the Supreme Court of Vermont recognized in *Wheeler,* even if the contested Vermont statute had imposed a confiscatory 100% tax rate, the total amount of Wheeler's Vermont tax liability would not have exceeded his Vermont income, and therefore the Vermont tax did not reach Wheeler's New Hampshire income. 249 A.2d at 890.

Furthermore, it is the Stevenses who ignore economic realities in asserting that Maine, which bases its tax rates for both residents and nonresidents on ability to pay, must ignore the Stevenses' actual ability to pay in this case:

> If a state resolves that it is appropriate for an individual who earns $100,000 to pay at the rate of $.25 on the dollar, it would appear to make no difference in terms of that determination whether the individual accumulated the sum by earning $100,000 in one state or $2,000 in fifty states. The argument for permitting a state to look to a taxpayer's total income from all sources for purposes of its progressive rate structure would therefore seem to be a logical corollary of the rationale for such a rate structure, a rationale that has essentially nothing to do with the territorial limits of the taxing state.

W. Hellerstein, *Some Reflections on the State Taxation of a Nonresident's Personal Income*, 72 Mich. L. Rev. 1309, 1323 (1974).

The Stevenses address equal protection and privileges and immunities only in a footnote, in which they assert that the requisite discrimination between similarly situated residents and nonresidents can be demonstrated if the term "similarly situated" is construed to require a comparison of the Stevenses with a Maine resident who has the same Maine income as the Stevenses but *no* non-Maine income. Pet. 6n.1. This position is supported only by the contention that inclusion of the Stevenses' non-Maine income in the comparison would be "unreasonable" because that income cannot be taxed by Maine. *Id.* However, logic dictates, and the Supreme Judicial Court of Maine held, that residents and nonresidents are similarly situated when they have the same *total* income. 571 A.2d at 1197 (Pet. 4a-5a); *see Wheeler v. State*, 249 A.2d 887, 889, 890-891 (Vt.), *appeal dismissed for want of a substantial federal question*, 396 U.S. 4 (1969).

The Stevenses, attempting to fit this case into the mold of *Austin v. New Hampshire*, 420 U.S. 656 (1975), now assert that retaliation by New Hampshire is likely if Maine's nonresident provisions are not declared unconstitutional. Pet. 8. However, the New Hampshire statute at issue in *Austin* was not found unconstitutional merely because it might have led to retaliation but because it discriminated between similarly situated residents and nonresidents. The Maine statute at issue here does not discriminate in this fashion. To suggest that Maine's statute should be invalidated merely because it is

politically unpopular in New Hampshire[3] and therefore might lead to retaliatory action by the New Hampshire legislature would make constitutional doctrine dependent upon the political attitudes of the New Hampshire electorate. The Constitution does not mandate the overturning of a nondiscriminatory tax law simply because the nonresident taxpayers prefer not to pay the full amount of the tax.

Finally, the Stevenses argue that Maine, by including a Maine nonresident taxpayer's New Hampshire income in the computation of his Maine income tax liability, somehow is exploiting New Hampshire's policy decision not to have a general personal income tax. Pet. 8-9. New Hampshire's tax policy, however, is, irrelevant to this appeal; Maine's measurement of a fair tax, reflecting ability to pay, on Maine income would be no different if New Hampshire had a broad-based personal income tax.[4] New Hampshire's current tax policy serves only to provide New Hampshire residents, who otherwise might be indifferent as to which of the two states taxes their income, with a personal financial stake in minimizing the tax that Maine imposes on their Maine income.

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[3] This political unpopularity is demonstrated by the legislation authorizing the New Hampshire attorney general to represent petitioners in this action. *See* N.H. Laws 1987, ch. 157.

[4] There is no valid reason why a New Hampshire resident's Maine income should be treated as the "low-bracket" income of that resident, thereby leaving his "upper-bracket" income for taxation by New Hampshire or his personal benefit, depending upon New Hampshire tax policy.

CONCLUSION

For the reasons stated above, the Court should deny the petition for writ of certiorari.

Respectfully submitted,

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Attorneys for Respondent

July 20, 1990

APPENDIX

U.S. Const., Art. IV, § 2, cl. 1

The Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in the several States.

U.S. Const., Amend XIV, § 1

All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

36 M.R.S.A. § 5111(4) (*repealed and replaced by* P.L. 1987, ch. 819, § 2)

A tax is imposed upon the Maine income of every nonresident individual. The amount of the tax shall be equal to the tax computed under this section and chapter 805 as if the nonresident were a resident, less applicable tax credits other than [the credit for income tax paid to another jurisdiction], and multiplied by the ratio of his Maine adjusted gross income, as defined in section 5102, subsection 1-C, paragraph B, to his entire federal adjusted gross income, as modified by section 5122.

36 M.R.S.A. § 5221(2) (Supp. 1989).

If both husband and wife are nonresidents and one has no Maine-source income, the spouse having Maine source income shall file a separate Maine nonresident income tax return, as a single individual, in which event his tax liability shall be separate; but they may elect to determine their joint taxable income as nonresidents, in which case their liabilities shall be joint and several.

If either husband or wife is a resident and the other is a nonresident, they shall file separate Maine income tax returns as single individuals, in which event their tax liabilities shall be separate; but they may elect to determine their joint taxable income as if both were residents and, in that case, their liabilities shall be joint and several.